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**In the
Supreme Court of the United States**

OCTOBER TERM, 1982

BRAEMOOR ASSOCIATES, a joint venture, and LAMBERT BERE, JR., OWEN HULSE, JR., CHARLES M. BENNETT, GEORGE JOUSMA, and WILLIAM J. KAYE, individually and as joint ventures doing business as Braemoor Associates,

Petitioners,

vs.

FEDERAL DEPOSIT INSURANCE CORPORATION,

Respondent.

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT**

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January 25, 1982

QUESTIONS PRESENTED

1. In these days of increasing court of appeals case-loads or at any time, can the court of appeals conduct what amounts to a trial de novo on law and facts ignoring the function of the district court judge and the record and using law not argued at the district court level and law not even argued at the court of appeals level or is such action so far a departure from the accepted and usual course of judicial proceedings as to cause reversal by the Supreme Court?
2. Does a court of appeals have the absolute discretion to apply law not argued below to the facts as some circuits hold, or can it only do so in exceptional circumstances as other circuits require?

PARTIES TO THE PROCEEDING

Only the parties listed in the case caption are parties to this proceeding. Other parties originally sued have previously been dismissed by the Federal Deposit Insurance Corporation.

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1. The decision below represents a decision of facts <i>de novo</i> as well as a decision based on law not argued in the District Court and law not argued in the Court of Appeals so as to displace entirely the function of the District Court in a manner which has so far departed from the accepted and usual course of judicial proceedings as to call for the exercise of this Court's power of supervision and this is especially true because it encourages the flood of appeals to the Court of Appeals for a trial <i>de novo</i>	10
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The petitioners Braemoor Associates, Lambert Bere, Jr., Owen Hulse, Jr., Charles M. Bennett, George Jousma and William J. Kaye respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit entered in this proceeding on August 13, 1982 and amended on October 28, 1982,

OPINION BELOW

The first opinion of the Court of Appeals is reported at 686 F.2d 550. The amended decision of the Court of Appeals and the Opinion of the District Court are unpublished and are reproduced at pages 32 and 1 of the appendix respectively.

JURISDICTION

The judgment of the Court of Appeals was entered on August 13, 1982. The judgment of the Court of Appeals was amended on October 28, 1982 in response to a timely petition for rehearing which was denied on that date, and this petition for a writ of certiorari was filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Illinois Revised Statutes (1981) Chapter 17, Section 37 states as follows:

§37. Loans to officers and loans on and purchases of bank's own stock.

(1) It shall not be lawful for a state bank to make any loan or extension of credit in excess of \$10,000 at any one time outstanding each to its president, or to any of its vice-presidents or its salaried officers or employees or directors or to corporations or firms, controlled by them, or in the management of which any of them are actively engaged, unless such loan or extension of credit and the provisions for the repayment thereof shall have been first approved, by the board of directors; provided that indebtedness of \$5,000 or less arising by reason of any general arrangement by which a bank makes payment to or on behalf of participants in a bank credit card plan,

check credit plan, interest bearing overdraft credit plan or similar open-end credit plan shall not be deemed an extension of credit for purposes of this Section; provided further that the provisions of Section 35.2 of this Act shall also be complied with to the extent, if any, that such provisions are applicable to such loan or extension of credit.

(2) It shall not be lawful for a state bank to make any loan or discount on the security of the shares of its own capital stock or preferred stock or on the security of its own debentures or evidences of debt which are either convertible into capital stock or are junior or subordinate in right of payment to deposit or other liabilities of the bank, nor to be the purchaser or holder of any such shares or securities, unless necessary to prevent loss upon a debt previously contracted in good faith; and stock or securities of the character aforesaid so purchased or acquired shall, within six months from the time of its purchase or acquisition, be sold or disposed of at public or private sale.

STATEMENT OF THE CASE

Defendant Braemoor Associates ("Braemoor") is a joint venture made up of seven individuals, with the five of those individuals who are currently living being defendants in this case. The Federal Deposit Insurance Corporation sued Braemoor and these individuals for collection of two loans it claimed it had bought from the State Bank of Clearing which was in receivership. Jurisdiction of that suit in the United States District Court was based on 12 U.S.C. §1819. After amendments to the complaint and stipulations, only two loans remained at issue in the case, namely a \$60,000 and a \$240,000 loan which the Federal Deposit Insurance Cor-

poration ("FDIC") claimed were still outstanding and owing.

Braemoor Associates had as its purpose the purchase of real estate in Illinois for investment and resale. Braemoor financed its property acquisitions and improvements for the years prior to sale which were usually loss years by (1) borrowing on the value of the real estate, (2) the willingness of a contractor Seneca Petroleum Corporation to extend credit to Braemoor for in excess of \$400,000 for improvements (Stipulation attached as Exhibit A to Pretrial Order ("Stip.") Par. 14.1, transcript p. 133-144)(3) the borrowing power of individual joint venturers who were wealthy, and (4) sales of real estate which eventually brought in money to cover all expenses and to give profits with said money coming from contracts of sale which were generally oral with numerous purchasers. The individual joint venturers were not told where they should go to borrow money. Many joint venturers were old customers of the State Bank of Clearing and they had previously borrowed money from that bank. Paul Bere, a joint venturer, was then president of that bank. Certain joint venturers borrowed over \$500,000 from that bank which they then lent to Braemoor. Every single penny of those loans has been paid back to the State Bank of Clearing and those loans are not the subject of this lawsuit. Braemoor also borrowed over \$750,000 from the Chicago City Bank which was a bank that was not related to the State Bank of Clearing. Those loans are in no way at issue in this case.

The State Bank of Clearing had a favored relationship with a man named Ringbloom and with 6 entities controlled by him and with officers of those entities. Ringbloom was a contractor and a real estate developer. Ring-

bloom and his companies were permitted to have huge overdrafts in their checking accounts at the State Bank of Clearing. Checks for Ringbloom and his entities would clear without there being funds in their checking accounts to pay those checks. Overdrafts on the checking accounts of \$10,000 were common and overdrafts of as much as \$71,000 occurred in those accounts. Ringbloom, his entities and his officers had millions of dollars of loans with the State Bank of Clearing. Examples of these loans and of overdraft balances are contained on Exhibits B and C of the Stipulation. In fact, when the State Bank of Clearing was closed, Ringbloom and related entities had loans and overdrafts that were stated by the FDIC to total \$4,822,455.16. (Stip. Par. 3.5.2).

The facts now stated relate to the \$60,000 loan which is one of the two loans that are the subject of the suit. Ringbloom approached Paul Bere wanting to purchase from Braemoor land on which to build condominiums. The sales price was \$400,000 and the first payment on that price amounting to \$60,000 was made in September of 1971. (Stip. par. 36.1) Although at the trial Ringbloom did not recall whether he had a payment schedule, joint venturer Hulse recalled that the next \$60,000 payment was due in January of 1972. (Tr. p. 107, 106). To make that payment, Ringbloom went to the State Bank of Clearing and borrowed the \$60,000 in a loan that was collateralized by stock which was stated on the loan minutes of the State Bank of Clearing to be worth \$285,000. (Tr. p. 56, Stip. par 26). That loan was a six-month loan and the FDIC is trying to collect that loan from Braemoor and its members though they did not borrow that money and are not a part of Ringbloom's entities. The reason for the FDIC trying to collect from Braemoor

is that the loan proceeds were used to purchase property from Braemoor. As the six-month loan maturity was expiring, Ringbloom paid off the \$60,000 loan by paying it from \$800,000 of loans that he got for a 10-day period from another bank. Those loans were in turn paid off with an \$800,000 loan that Ringbloom entities got from the State Bank of Clearing. (Stip. par. 29.1-29.4). The loan ledger at the State Bank of Clearing shows the \$60,000 loan as paid. (Stip. par. 26.5) That loan had been approved by the Board of Directors of the State Bank of Clearing. (Stip. par. 26.4). At the time Braemoor got the \$60,000 from Ringbloom on Ringbloom's purchase of land on which condominium units were built, Braemoor was not pressed for money and in fact could easily have gotten \$60,000 or more from the Chicago City Bank where it had paid down one of its loans by \$175,000 and where joint venturer Hulse's company had 1.2 million dollars in short term deposits. (Tr. p. 145, 134).

It is to be noted that Braemoor had no ownership interest in Ringbloom's entities and Ringbloom had no ownership interest in Braemoor.

The \$240,000 loan will now be discussed. In July of 1972 Ringbloom approached Paul Bere and made an offer to purchase several 20-acre tracts of land at \$240,000 per tract from Braemoor and he purchased the first tract for \$240,000 in that month. (Tr. p. 148-149). Unknown to defendants in this lawsuit, the \$240,000 came from a blank note that joint venturer Lambert Bere had left with his brother Paul Bere for family business six months to a year earlier which Paul Bere filled in for \$417,000 and presented to the Board of the State Bank of Clearing which approved the loan. The \$417,000 passed to Ringbloom without Lambert sign-

ing any checks because Paul used bank debit memos. Ringbloom used the entire \$417,000 with \$240,000 of that sum going for the purchase of a 20-acre parcel of real estate from Braemoor. That note was filled in and the \$417,000 loan was obtained on the same day that Paul Bere got Ringbloom's entities \$800,000 in 10-day loans from another bank which means Ringbloom's entities got \$1,217,000 on loan transactions on that day alone through Paul Bere. (Stip. par. 29.1, 38). Within 21 days the \$417,000-loan on the filled-in note was fully paid from proceeds of \$780,000 in other loans that the Ringbloom entities got from the State Bank of Clearing. (Stip. par. 41-42.1). The loan ledger of the State Bank of Clearing states that the \$417,000 loan has been paid. (Stip. par. 38.6). The FDIC is seeking to collect \$240,000 of the \$417,000 loan that *has been paid* from other loans Ringbloom obtained because Ringbloom used the \$240,000 to purchase a 20-acre parcel from Braemoor, claiming that Paul Bere was involved on too many sides of the transaction. Added to this is the fact that Paul Bere was a secret partner of Ringbloom's in that purchase at the time he recommended that Braemoor sell the land to Ringbloom. (Tr. p. 147, 153). At the time that Braemoor got the \$240,000 for the sale of the land, it was under no pressure from a corporate creditor to whom it paid that money after receiving it. (Tr. p. 134). That creditor had an excellent cash position at that time. (Tr. p. 134).

The trial of the case proceeded with a 45-page stipulation of facts plus the testimony of about 11 witnesses. After plaintiff rested, defendants moved for judgment under Rule 41(b) of the Federal Rules of Civil Procedure. The trial stopped, arguments were heard and a briefing schedule was set up. The District Court judge

then wrote a 19-page opinion dismissing the case and in that opinion the judge found that the two loans in question were made for the purchase of property for Ringbloom rather than as a device for financing Braemoor. He further found that the testimony of defendants was credible and that they had no actual or constructive knowledge of these two loan transactions or of Paul Bere's actions with regard to those loans for Ringbloom and further that defendants had not expressly or impliedly delegated to Paul the task of financing any purchaser purchasing land from Braemoor. The judge also found that defendants had sufficient sources of credit other than the State Bank of Clearing to meet their obligations as they became due. (Findings of Fact paragraphs 62-71 in the district Court Opinion).

The FDIC then appealed to the Seventh Circuit which reversed the District Court. That opinion noted that there was no per se prohibition in Illinois against banks loaning their officers money or lending money to entities wherein an officer had any management responsibilities. However, the Court of Appeals referred to a statute never argued by any party at any level which said officers could not approve such loans if they were over \$10,000, but rather such loans had to be approved by the board of directors of the bank. The Appeals Court said that the loans were really not for the purpose of aiding a purchaser of real estate, but instead were actually loans to Braemoor and since such loans had not been approved by the bank board of directors they were considered to be fraudulently obtained and that fraud in not following the statute would be imputed to Braemoor and its members. However, contrary to that Court of

Appeals decision the parties had entered into a stipulation that was uncontradicted that stated that the loans had indeed both been approved by the bank's board of directors. A motion for rehearing was timely filed based on that fact and other claimed errors as to fact and law and as to the functions assumed by the Court of Appeals.

The Court of Appeals then amended its decision. It changed numerous facts. It still centered around the same statute, but this time it said that it was implicit in the terms of that statute that any conflict of interest had to be disclosed to the bank board when it considered the loans. It cited no decision supporting that implicit requirement. It still considered the loans to really be loans to Braemoor and stated that the loans did not involve financing any purchaser's of Braemoor real estate, but rather on page 11 it held the loans were for a street and sewer system on property owned by Braemoor. Since Paul Bere had not disclosed his conflict of interest to the bank board as to a relationship as a joint venturer, it said the loan had been obtained by fraud which would be imputed to Braemoor and its members. The Findings of Fact of the Court of Appeals in both opinions differed greatly from the Findings of Fact of the District Court. The Court of Appeals did not find that the Findings of Fact of the District Court were clearly erroneous.

REASONS FOR GRANTING THE WRIT

I. THE DECISION BELOW REPRESENTS A DECISION OF FACTS *DE NOVO* AS WELL AS A DECISION BASED ON LAW NOT ARGUED IN THE DISTRICT COURT AND LAW NOT ARGUED IN THE COURT OF APPEALS SO AS TO DISPLACE ENTIRELY THE FUNCTION OF THE DISTRICT COURT IN A MANNER WHICH HAS SO FAR DEPARTED FROM THE ACCEPTED AND USUAL COURSE OF JUDICIAL PROCEEDINGS AS TO CALL FOR THE EXERCISE OF THIS COURT'S POWER OF SUPERVISION AND THIS IS ESPECIALLY TRUE BECAUSE IT ENCOURAGES THE FLOOD OF APPEALS TO THE COURT OF APPEALS FOR A TRIAL *DE NOVO*.

The Court of Appeals was grossly indifferent to the facts in the record of the District Court and its crucial "facts" in its opinion were not facts. This can most easily be demonstrated regarding the cornerstone fact of its first opinion. It held that fraud was attributed to the defendants due to the fact that the two loans involved had not been approved by the Board of Directors of the State Bank of Clearing as required by Illinois law. Diametrically opposite to this "fact" was the written stipulation of fact by the parties that in paragraph 55 clearly stated that such loans had in fact been approved by the Board of Directors of the State Bank of Clearing. Had it not been for that "fact", defendants would have had no liability under the reasoning of the first decision of the Court of Appeals and the District Court would not have been reversed. There were numerous "facts" stated in that first decision that were not facts in the

record. The petition for rehearing brought out such obvious errors to the Court of Appeals that it had to amend its decision to correct some of its errors as to facts. But in doing so, it adapted "facts" to bolster its legal theory that were not facts in the record and created a trial *de novo* on the facts absent the presence of witnesses and with blindness toward a 45-page written stipulation of facts contained in the pretrial order.

This Court has held that "It is not enough that we (the Supreme Court or an appellate court) might give the facts another construction, resolve the ambiguities differently, and find a more sinister cast to actions which the district court apparently deemed innocent. We are not given those choices because our mandate is not to set aside findings of fact 'unless clearly erroneous'." *United States v. Realty Board*, 339 U.S. 485 at 495-6 (1950). The Court of Appeals in the case presently before this Court even went beyond that restriction and "facts" that were truly nonexistent were used which went to the heart of its amended decision.

The amended decision continued to rely on the following Illinois statute which had never been cited by any party at the district court level and had never been cited by any party at the appeals court level:

"It shall not be lawful for a state bank to make any loan or extension of credit in excess of \$10,000 at any one time outstanding each to its president or to any of its vice-presidents or its salaried officers or employees or directors or to corporations or firms controlled by them or in the management of which any of them are actively engaged, unless such loan or extension of credit and the provisions for the repayment thereof shall have been first approved, by

the board of directors". (Ill. Rev. Stat., 1981, ch. 17
§ 347(1))

The amended decision stated that this language implicitly required the officers to disclose any conflict of interest in a loan and if that conflict of interest was not disclosed, the loan was fraudulently procured. The statute does not say that and there are no cases in the annotation of that statute which state that "implicit" requirement. Further, that statute causes no liability to defendants under the true facts of the case. The Appeals Court treats the loans to the Ringbloom entities so Ringbloom could purchase property from Braemoor as involving the "laundering" of money which in "fact" constituted loans to Braemoor Associates. The Appeals Court specifically stated at page 557 of the published opinion in 686 F.2d 550 and repeated in the amended opinion the following language: "The loans in issue were not for the purchase of any properties; they were for a street and a sewer system on property already owned by Braemoor". Thus, the Court of Appeals is saying that the Illinois statute applies because the loans are loans to Braemoor and not loans to Ringbloom for him and his entities to purchase property from Braemoor. In finding of fact 69, the District Court found the opposite was true, namely that "The loan transactions at issue were made for the purchase of property (by Ringbloom) rather than as a device for the purpose of financing the Braemoor partnership." The record backs the District Court finding rather than the Court of Appeals fiction. In paragraph 36.1 of the stipulation of facts that is Exhibit A to the Final Pretrial Order in the District Court the parties stipulated that the \$60,000 involved was a payment by Western to Braemoor Associates with

respect to the purchase of the Condo property upon which it (Western, which is a Ringbloom entity) later built 88 condominium units. And as to the \$240,000, Ringbloom testified he used it in July of 1972 to purchase 20 acres of land from Braemoor. (Tr. p. 148-9) Thus, the District Court's finding is based on fact and the loans were to Ringbloom and his entities, rather than being a loan to Braemoor, and the Illinois Banking Statute intended to apply because the Court of Appeals thought of it as a loan to Braemoor does not even apply to this case. Furthermore, these loans have been paid as shown in the Statement of the Case and no one has any liability for these loans, a fact ignored by the Court of Appeals.

The Court of Appeals also tried to make it appear that Braemoor forced these loan transactions because it needed a source of money to pay its bills. That is contrary to finding of fact 71 by the District Court which held that, "At the time of the transactions at issue, the defendants, both in their individual capacities and as a partnership, had sufficient sources of credit other than the State Bank of Clearing to meet their obligations as they became due." For instance, Braemoor could have easily obtained money from the Chicago City Bank where its loan of \$500,000 had only \$375,000 outstanding, according to Hulse, whose company was that bank's large depositor with \$1,200,000 in 30-day CD's at that bank. (Transcript p. 145, 134).

It is also noted that the District Court judge who saw the witnesses as they gave their testimony found at finding of fact paragraph 62 that "the court finds the testimony of all of the defendants is credible". That judge also found at findings of fact 63 through 70 that the

defendants did not participate in the loan transactions, did not have express or constructive knowledge of what occurred, and did not expressly or impliedly delegate to Paul Bere to arrange financing to Ringbloom or his entities for purchases from Braemoor. The record also is clear throughout that Braemoor was not in the ordinary course of business getting financing for its purchasers. The testimony and stipulation support the findings of the District Court. The Appellate Court did not find these findings clearly erroneous. Instead, it substituted its own "off-the-wall" findings of fact, and law that no one had ever argued at any level, and rendered a decision that was a *de novo* decision and thus so far departed from the accepted and usual course of judicial proceedings as to call for the exercise of this Court's power of supervision.

It is also noted that the banking law applied to the case was applied only on the appeals court's own motion, and as Judge Learned Hand stated, "It is only an 'egregious kind of error' (that) we may consider on our own motion". *Scott v. Central Commercial Co.*, 272 F.2d 781 at 782-3 (2nd Cir., 1959). Such a situation is not involved in this case.

The Justices of this Court have been making pronouncements publicly as to ways to cope with the rising case loads of the federal court system. Getting the trial bar back to basic requirements of trial in the District Court is a clear way to help the situation. It should be known that a case brought in the United States District Court should be fully prepared on the facts and the law if it is taken to trial and that the United States Court of Appeals are not going to be "a second-guess heaven". This Court's power of supervision should be

exercised to enforce this point as well as to give the due respect to the district court judges who deal with arguments before them and who have the fact finding power.

II. THE DECISION BELOW CONFLICTS WITH DECISIONS OF OTHER CIRCUITS AS TO THE EXERCISE OF DISCRETION BY APPELLATE COURTS TO CONSIDER MATTERS NOT CONSIDERED BY THE DISTRICT COURT.

This reason goes beyond the *de novo* fact and law trial discussed above and refers to the Seventh Circuit applying for the first time a banking statute never referred to in the District Court or even referred to by the parties in the appeals court. In *Singleton v. Wulff*, 428 U.S. 106 at 121 (1976), this Court stated, "The matter of what questions may be taken up and resolved for the first time on appeal is left primarily to the discretion of the courts of appeals, to be exercised on the facts of individual cases. We announce no general rule. Certainly there are circumstances in which a federal appellate court is justified in resolving an issue not passed on below, as where the proper resolution is beyond any doubt, or where 'injustice might otherwise result.'" Most courts of appeals hold after that decision that they will consider something not raised in the district court only under extraordinary circumstances. *Journey v. Vitek*, 685 F.2d 239 at 243 (8th Cir. 1982), *Needleman v. Bohlen*, 602 F.2d 1 at 4 (1st Cir., 1979). However, the ninth circuit holds that *any* pure question of law that does not cause the parties to develop new or different facts can be raised in the court of appeals for the first time without limitation. *Commodity Future Trading Commission v. Co. Petro Marketing Group, Inc.*, 680 F.2d 573 at 581 (9th Cir. 1982). These positions are quite different.

Because there are no extraordinary circumstances in the case now before this Court, the Seventh Circuit had to be adopting the Ninth Circuit rational which freely permits raising new law issues for the first time in the court of appeals, based on the fact situation in the District Court, although the Seventh Circuit mangled the fact situation in the District Court. It is maintained that the Ninth Circuit position as adopted here is too broad for it opens the courts of appeals to liberal second guessing on new legal theories at the appeals levels whereas counsel really should have the obligation to fully express their reliance on points of law at the district court level except in extraordinary circumstances which certainly do not exist in the case currently before this Court. That conflict between the circuits should be resolved.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgments and opinions of the Seventh Circuit as amended.

Respectfully submitted,

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JANUARY 25, 1983

APPENDIX

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

FEDERAL DEPOSIT INSURANCE
CORPORATION,

Plaintiff,

vs.

BRAEMOOR ASSOCIATES, a
joint venture, et al.,

Defendants.

NO. 76 C 3295

Before the Honorable
Nicholas J. Bua, Judge
United States District Court

O R D E R

The matter before the court arises out of an action brought by the plaintiff, the Federal Deposit Insurance Corporation, against the defendants, Braemoor Associates, Lambert Bere, Jr., Owen Hulse, Jr., Charles M. Bennett, George Jousma and William J. Kaye, seeking the recovery of damages under theories of breach of trust, conspiracy, and unjust enrichment. The jurisdiction of the court is founded upon Title 12 U.S.C. § 1819. The matter at bar was tried by the court. At the close of the plaintiff's case, the defendants moved, pursuant to Rule 41(b), Fed. R. Civ. P., for involuntary dismissal of the claim. This court, after having reviewed the evidence presented at trial and the arguments of the parties, believes that dismissal of the plaintiff's claims is warranted. For this reason, the plaintiff's action is dismissed. In conjunction with this ruling, the court makes the following findings of fact and conclusions of law.

FINDINGS OF FACT

For brevity, the following persons and entities will be referred to herein as follows: Paul R. Bere ("Paul"); Lambert Bere, Jr. ("Lambert"); Owen Hulse, Jr. ("Hulse"); Charles M. Bennett ("Bennett"); William J. Kaye ("Kaye"); Allan Gustafson ("Gustafson"); David Mayes ("Mayes"); LaSalle National Bank of Chicago as Trustee under Trust No. 24786 ("LaSalle LT 24786"); Chicago City Bank and Trust Company of Chicago, individually and as Trustee under Trust Nos. 8825 and 8972 ("Chicago City Bank LT 8825" and "Chicago City Bank LT 8972", respectively); Seneca Petroleum Company ("Seneca"); Kenneth Ringbloom ("Ringbloom"); and Western Land Planning Company ("Western").

1. At all relevant times herein until his death on July 26, 1974, Paul was President, a Director and the Chairman of the Board of Directors of the State Bank of Clearing (the "Bank"), an Illinois banking corporation located at 5235 West 63rd Street, Chicago, Illinois. Lambert was a Director of the Bank from and after January, 1973. He began working at the Bank as a vice-president in August, 1974, was formally elected a vice-president by the Board of Directors in January, 1975, and continued to serve as vice-president until the Bank closed.

2. On July 12, 1975, the Illinois Commissioner of Banks and Trust Companies took possession and control of the State Bank of Clearing, its assets and affairs, and appointed the FIDC as Receiver thereof. A Complaint for Dissolution of the Bank was filed in the Circuit Court of Cook County, Illinois and was assigned Case No. 75 CH 4407. Pursuant to statutory authorization

and the approval of the Circuit Court of Cook County, the Receiver transferred certain of the assets owned by the Bank, including those at issue herein, to the FDIC in its corporate capacity.

3. At the time of the transactions in issue:

(a) Paul and Bennett were partners in the BEB partnership and were co-owners of property on Wise Road in Schaumburg, Illinois.

(b) Paul and Bennett were financially interested in Universal Wood Products.

(c) Paul, Bennett, Lambert and Kaye were co-investors in property referred to as the Roberts Road property.

(d) Paul, Lambert and Bennett jointly owned the Cornell Farm.

(e) Paul and Bennett each owned a 1/8th interest in the Briarcliff Apartments.

(f) Paul was a limited partner in Shore Heights Village Apartments, of which Ringbloom was one of the general partners and Western (100% owned by Ringbloom) was another limited partner.

(g) Paul and Ringbloom were partners in Ken Enterprises.

(h) Paul, Lambert, George Jousma and Richard Jousma were partners in View Enterprises and were jointly liable to Sam Pancotto for a \$300,000 loan.

(i) Paul and Hulse were joint purchasers of certain property in Carol Stream, Illinois.

(j) Hulse, Lambert and View Enterprises [see (h) above] were co-lenders, at Paul's request, to Western Land Acquisition Company, a company owned by Ringbloom.

4. From time to time, Kaye, Bennett, Richard Jousma, George Jousma and Lambert, at Paul's request, signed promissory notes in blank as to date and amount, and left such notes in Paul's possession.

5. On December 31, 1968, Gustafson, Mayes, Kaye and Lambert as purchasers, and LaSalle LT 24786 as seller, executed an Agreement for-Deed, for the purchase of 146 acres in DuPage County referred to as the "Braemoor Farm" or "the Farm". The Agreement for Deed required the purchasers to pay a total purchase price of \$718,000 in installments, including a down-payment of \$100,000 and installments of \$100,000 each on the first day of October of 1970 through 1975, plus interest of 6-3/4% on the unpaid principal balance.

6. In April, 1969, Mayes, as purchaser, executed a Contract for the purchase of approximately 12 acres of property generally referred to as the Condominium or "Condo" property for \$74,500.

7. On July 21, 1969, Mayes and Gustafson as "Developers" entered into an Annexation Agreement with the Village of Burr Ridge with respect to the Farm, the Condominium property and additional land referred to as the Braemoor Estates property.

8. Paragraphs 7A and 9 of the Annexation Agreement required the Developers to furnish a water system, including a 250,000 gallon water storage tank, for the property and convey the water system to the Village, build two Olympic size swimming pools and a recreational building on the property, and donate 8 lots to the Village.

9. Between April 22, 1969 and May 19, 1970, Paul approved and caused the Bank to make loans totalling \$399,000 on notes signed by Mayes, Kaye, Richard Jousma and Gustafson. The loan proceeds were used to pay in part for the Farm, Condominium and Braemoor Estates properties. All of these loans have been repaid.

10. On June 30, 1970, Hulse, Bennett, Kaye, Richard Jousma, Lambert and Paul executed the Braemoor Associates Joint Venture Agreement ("Joint Venture Agreement"). Richard Jousma signed the Joint Venture Agreement on behalf of himself and George Jousma, each of whom had a one-twelfth (1/12th) interest in the joint venture. Each of the other joint venturers had a one-sixth interest.

11. Paul invited the others to join the joint venture and drafted the Joint Venture Agreement.

12. The only capital contributed to Braemoor Associates was \$3,000, consisting of \$500 paid by each member, except the Jousmas who paid \$250 each. The members of Braemoor Associates were generally wealthy.

13. Braemoor Associates assumed the obligations of the borrowers to the State Bank of Clearing for the loans set forth in paragraph 9 hereof.

14. Braemoor Associates also assumed the obligation of Paul to the Argo State Bank in the amount of \$50,000, which had been used for the acquisition of the subject real estate and which was subsequently repaid by Braemoor Associates.

15. Braemoor Associates assumed the obligations of Mayes and Gustafson as "Developers" under the Annexation Agreement referred to in paragraph 7 hereof.

16. Gustafson and Mayes assigned their interest in the Agreement for Deed for the purchase of the Farm property to Braemoor Associates, and Braemoor Associates assumed the obligations of the purchasers under that Agreement.

17. On July 6, 1970, Braemoor Associates and Seneca entered into an Agreement for the construction of sewers, streets and other improvements on the Braemoor Estates property. Hulse was president of Seneca. The Agreement estimated the cost to be approximately \$522,000. The final cost of the work was approximately \$647,000.

18. As security for their obligation to Seneca, Braemoor Associates conveyed lots 27 to 67 in Braemoor Estates into Chicago City LT 8972, in which Seneca owned 100% of the beneficial interest and Hulse held the power of direction. Under the Agreement, Braemoor Associates was required to pay Seneca the cost of construction, or \$15,000 per lot, in order to withdraw the lots from the Trust.

19. On July 24, 1970 and October 2, 1970, Paul approved and caused the Bank to make loans of \$24,000 and \$100,000 on notes signed by Bennett and George Jousma, respectively. The loan proceeds were used for the benefit of Braemoor Associates. The loans have been repaid.

20. On December 15, 1970, Chicago City Bank made a loan of \$500,000 to Braemoor Associates. The maturity date of this loan was December 15, 1972. The loan balance on this loan was \$325,000 on March 15, 1971, and it was reduced to \$312,500 on July 7, 1972. It was fully repaid on November 3, 1972.

21. The Chicago City Bank loan was secured by a pledge of the beneficial interest in Chicago City Bank LT 8825, which held title to Lots 1-4 and 6-26 in Braemoor Estates.

22. The proceeds of the Chicago City Bank loan were deposited into the Braemoor Associates' checking account at Chicago City Bank. On December 14 and 15, 1970, Braemoor Associates drew checks to repay \$321,500 of the Bank's loans; to pay interest totalling \$64,213.64 on the Bank's loans and the Agreement for Deed; and to pay other obligations assumed by Braemoor Associates. The total of the checks drawn by Braemoor Associates was \$529,039. As a result, Braemoor's account was overdrawn from December 15, 1970 until February 24, 1971, when the ~~proceeds of the Bank's~~ \$55,000 loan to Kaye were deposited into the account.

23. Paul approved and caused the Bank to make loans of \$78,4000 to Bennett on January 20, 1971; \$55,000 to Kaye on February 24, 1971; \$100,000 to George Jousma on June 4, 1971; and \$20,000 to Bennett on June 18, 1971.. All of the loan proceeds were used for the benefit of Braemoor Associates. These loans have been repaid.

24. On July 20, 1971, the Braemoor Associates entered into an Agreement to purchase a water system, including a water tower tank, from the Hinsdale Industrial District for \$230,000 and signed Notes to evidence their liability under the Agreement. The dates of the payments due under the Agreement and the dates of the payments made by or on behalf of Braemoor Associates are as follows:

<u>Amount</u>	<u>Due On Or Before</u>	<u>Paid</u>
\$60,000	Closing	8-23-71
60,000	12-31-71	1-14-72
60,000	6-30-72	6-30-72
50,000	12-31-72	11-17-72

25. The above Agreement further provided that if the property on which the water system was located was not annexed to the Village of Burr Ridge within one year, the Braemoor Associates were liable to pay an additional \$100,000. Braemoor Associates entered into the Agreement in order to satisfy the obligation imposed on the "Developer" by paragraph 7A of the Annexation Agreement to acquire and convey to the Village of Burr Ridge a water system; including a water tower tank, at no cost to the Village of Burr Ridge.

26. Paul handled the negotiations for and drafting of the above Agreement, and arranged for the signing of the Agreement and Notes by the Braemoor Associates. Paul paid the first installment of \$60,000 personally, and was later reimbursed by Braemoor Associates on September 30, 1971.

27. On August 23, 1971, Paul approved and caused the State Bank of Clearing to make a loan of \$17,350 to Kaye. The proceeds of this loan were paid over by Kaye to Braemoor Associates for the purchase of a lot in Braemoor Estates. This loan was repaid.

28. In or about September, 1971, Paul and Ringbloom had discussions concerning the sale of the Condominium property. As the result of these discussions, an oral agreement was reached for the sale of the Condominium property to Western for \$400,000, and Western paid \$60,000 to Braemoor Associates on September 29, 1971, as an earnest money deposit.

29. Western made additional payments to Braemoor Associates of \$60,000 on January 14, 1972, \$80,000 on June 30, 1972, and a final payment of \$200,000 on October 27, 1972 for the Condominium property.

30. On January 10, 1972, Paul approved and caused the State Bank of Clearing to make a loan of \$60,000 to Ringbloom. At this time, Ringbloom individually had unpaid loans totalling \$444,721.84 from the State Bank of Clearing.

31. The proceeds of this loan (together with the proceeds of a \$165,000 loan which is not in issue) were deposited into the checking account of Western at the State Bank of Clearing on January 10, 1972. The balance in Western's account before the deposit of these funds was \$18,931.78, less any outstanding checks. After said deposit and the payment of checks presented that day, the balance in Western's account was \$233,249.43.

32. Western drew a check dated January 10, 1972, on its account for \$60,000 payable to the order of Braemoor Associates, and on January 14, 1972 Hulse endorsed and deposited this check into Braemoor's checking account. This payment was reflected on Western's books and records and Braemoor Associates' records as the second partial payment by Western to Braemoor Associates of the purchase price for the Condo property.

33. Western would not have made the \$60,000 payment to Braemoor Associates if the Bank had not made the \$60,000 loan.

34. On January 14, 1972, Hulse and Paul drew a check on Braemoor Associates' account for \$60,000 in payment of the \$60,000 installment due for the water system. The check was mailed on January 19, 1972, to make that payment. After the foregoing transactions, the balance in the Braemoor Associates' checking account was \$1,874.33.

35. In May, 1972, Illinois and Federal Reserve System bank examiners computed the total outstanding loans to Ringbloom,

Western, and certain other related entities to aggregate in excess of \$1,895,000.

36. On or about July 14, 1972, Paul requested Marquette National Bank to make loans totalling \$800,000 to Ringbloom and Western, to be used to repay in part the Ringbloom loans. Paul gave the Marquette National Bank written assurance that within 10 days the State Bank of Clearing would again lend Ringbloom at least \$800,000 to enable him to repay the Marquette National Bank loans. --

37. On July 14, 1972, the Marquette National Bank made a \$400,000 loan to Western and a \$400,000 loan to Ringbloom, neither of whom had previously been a customer of that bank. The loan proceeds were disbursed by checks deposited directly into the respective checking accounts of Western and Ringbloom at the State Bank of Clearing.

38. On July 24, 1972, the State Bank of Clearing made a loan of \$335,000 to Ringbloom and a loan of \$465,000 to Western. The loan proceeds were used to repay the two \$400,000 loans owed to the Marquette National Bank. Specifically, the proceeds of the \$335,000 loan were deposited into Ringbloom's account along with a check of Western's payable to Ringbloom for \$65,000 (drawn out of the proceeds of Western's \$465,000 loan). The total of \$400,000 was then transferred by a debit memo to the Marquette National Bank.

39. On June 27, 1972, the balance in Braemoor Associates' checking account was \$22,070. On or before June 30, 1972, Braemoor Associates was obligated to pay the following debts:

(a) \$14,107.50 to LaSalle LT 24786 for interest due on the unpaid balance under the Agreement for Deed;

(b) \$60,000 to Hinsdale Industrial District for the water tower pursuant to the Agreement and Note; and

(c) \$12,500 to Chicago City Bank on its loan.

40. On June 26, 1972, Paul approved and caused the State Bank of Clearing to make a \$25,000 loan to Charles R. Smith, an officer of Western, and on June 30, 1972, Paul approved and caused the State Bank of Clearing to make a \$48,000 loan to View Enterprises (owned equally by Paul, Lambert and the two Jousmas). The proceeds of these loans were credited to Western's checking account at the State Bank of Clearing on June 30, 1972. Immediately prior to this deposit, Western's account had an overdraft balance of \$10,568.61.

41. Western drew a check dated June 26, 1972, on its account payable to Braemoor Associates for \$80,000, and Braemoor Associates deposited the check into its account on June 30, 1972. This payment was reflected on Western's records as the third partial payment by Western to Braemoor Associates for the Condo property.

42. On July 5, 1972, the proceeds of the Smith loan were transferred out of Western's account to Smith's account, an additional \$35,000 was paid on other Western checks and the said \$80,000 check was paid, all of which created an overdraft in Western's checking account at the State Bank of Clearing in the amount of \$52,797.47 on July 5, 1972.

43. On June 30, 1972, Paul and Hulse drew checks on the Braemoor Associates' checking account to pay LaSalle LT 24786 \$14,107.50 for interest due under the Agreement for Deed and to pay Hinsdale Industrial District \$60,000 due under the Agreement for the water tower and system.

44. Sometime prior to July, 1972, Paul and Ringbloom discussed the sale of the Farm property. As the result of these discussions, Paul and Ringbloom orally agreed that Braemoor Associates would sell, and Ringbloom or Western would buy, the Farm property in 20 acre increments for \$12,000 per acre. There has never been any written contract reflecting the terms of this agreement. No specific dates for payment were fixed by the oral agreement, except that Western would make at least one 20-acre purchase in approximately October of each year in order to furnish Braemoor Associates with the funds needed to make its annual \$100,000 payment of principal, plus interest, to LaSalle LT 24786 for the Farm property.

45. As of July, 1972, Braemoor Associates owed Seneca over \$436,000 for sewers, streets and other improvements constructed by Seneca on the Braemoor Estates property, pursuant to the Seneca contract of July 6, 1970. As of July, 1972, Braemoor Associates had sold 12 of the lots pledged to Seneca to secure the payments due under the Seneca contract, and was about to sell 4 more of the pledged lots to third parties. Under the Seneca contract, Braemoor Associates were required to pay Seneca \$240,000 (\$15,000 per lot) to obtain the release of the 16 lots from the pledge. Braemoor Associates, however, had insufficient funds available to pay Seneca to obtain the release of the lots, and Hulse, as president of Seneca, released the 12 lots without requiring prior payment.

46. As of July, 1972, Indian Trails Apartments, a Ringbloom venture, owed the State Bank of Clearing \$167,567.71 on three loans.

47. On July 14, 1972, Paul approved and caused the State Bank of Clearing to make a loan of \$417,567.71 to Lambert on a note which Lambert had signed in blank at Paul's request and left with Paul. The proceeds of the loan were credited to Lambert's checking account at the State Bank of Clearing. On July 17, 1972, the State Bank of Clearing, at Paul's direction, transferred \$167,567.71 out of Lambert's checking account to pay the three Indian Trails Apartments loans, and transferred the remaining \$250,000 from Lambert's checking account to Western's checking account at the State Bank of Clearing. Lambert did not owe Western \$250,000, or any other amount. Prior to such transfer, Western's checking account had an overdraft balance of \$26,263.

48. On July 17, 1972, Western paid \$240,000 of the above \$250,000 to Braemoor Associates, after which Western's checking account was again overdrawn by \$12,972.50. On July 25, 1973, Braemoor Associates paid this \$240,000 to Seneca.

49. On August 1, 1972, Paul caused the State Bank of Clearing to make a \$500,000 loan to Albany Supply Company (which was wholly owned by American Contractors, Inc., which was wholly owned by Western of which Ringbloom was the sole shareholder) and a \$150,000 loan to Ringbloom Construction Company (which was also owned by Ringbloom).

50. On August 1, 1972, Albany Supply Company and Ringbloom Construction Company each paid \$125,000 of these loan proceeds to Western. Prior to this deposit, Western's account was overdrawn in excess of \$18,000.

51. Western issued its undated check for \$250,944.45 payable to Lambert. Paul caused this check to be credited to

Lambert's checking account at the State Bank of Clearing. After these transactions, Western's checking account was again overdrawn in excess of \$37,000.

52. Paul then caused the State Bank of Clearing to transfer the said \$250,944.45 out of Lambert's checking account to pay part of Lambert's July 14, 1972 loan. The above Albany Supply Company and Ringbloom Construction Company loans remain unpaid.

53. The \$165,567.17 balance of the Lambert loan was paid with the proceeds of three new loans which Paul caused the State Bank of Clearing to make to Indian Trails Apartments on August 2, 1972. These three loans were also acquired by the FDIC in the transaction described in paragraph 2 above, and FDIC has settled them for \$125,000.

54. Braemoor Associates owed Chicago City Bank \$28,000 for accrued interest by October 31, 1974. However, from October 14, 1974 through October 29, 1974, Braemoor Associates had only \$2,891.82 in its checking account.

55. On October 30, 1974, Lambert permitted the State Bank of Clearing to make a \$36,500 loan to Kaye, the proceeds of which were deposited into Kaye's business account at the State Bank of Clearing.

56. On October 31, 1974, Kaye paid \$32,000 of the \$36,500 loan proceeds to Braemoor Associates and \$4,369.88 of the proceeds to the State Bank of Clearing for interest on a loan to Universal Art Products.

57. On October 29, 1974, Braemoor Associates drew a check for \$28,000 to pay Chicago City Bank for the accrued interest.

58. Kaye's purpose in obtaining the October 30, 1974 loan was to enable Braemoor Associates to pay the \$28,000 due to Chicago City Bank, and to enable Kaye to pay accrued interest on the Universal Art Products loan.

59. Braemoor Associates suffered losses in each year, except 1972, as follows:

1970 loss		(96,879)
1971 loss		(100,387)
1972	ordinary loss (239,182) capital gain <u>+490,732</u> net profit	251,548
1973	ordinary loss (320,125) capital gain <u>+128,460</u> net loss	(191,665)
1974	ordinary loss (61,356) capital gain <u>+ 1,237</u> net loss	(60,029)
1975 loss		<u>(87,358)</u>
	6-year ordinary loss (905,288) 6-year capital gain <u>+620,519</u> Net 6-year loss	(284,769)

60. The State Bank of Clearing did not have a loan committee which would review applications for loans at the time of these transactions.

61. Paul had exercised nearly exclusive control of the decision making process in rejecting or approving commercial loans at the State Bank of Clearing at the time of these transactions.

62. The court finds that the testimony of all of the defendants is credible.

63. The defendants had no actual knowledge of the loan transactions in issue.

64. The defendants did not participate in the loan transactions at issue.

65. The defendants had no actual knowledge of Paul's breach of his fiduciary duties to the bank.

66. The circumstances of the financial transactions between the defendants and Paul were not so extraordinary that the defendants should have known of Paul's breach of trust nor were the defendants in possession of such facts sufficient to alert a reasonable person to inquire whether Paul was breaching his trust.

67. The defendants did not expressly delegate to Paul the authority to arrange financing for the purchase of the Braemoor properties.

68. The defendants did not impliedly delegate to Paul the authority to arrange financing for the purchase of the Braemoor properties.

69. The loan transactions at issue were made for the purchase of property rather than as a device for the purpose of financing the Braemoor partnership.

70. There is no evidence of an agreement, either express or implied, between the defendants and Paul to conceal Paul's interest in the Braemoor partnership.

71. At the time of the transactions at issue, the defendants, both in their individual capacities and as a partnership, had sufficient sources of credit other than the State Bank of Clearing to meet their obligations as they became due.

CONCLUSIONS OF LAW

Count I, Plaintiff's Claim for the Imposition of a Constructive Trust

1. The plaintiff's burden of proof in an action which requests the court to impose a constructive trust requires that the plaintiff prove its case by evidence which is "so strong, unequivocal and unmistakable as to lead to one conclusion."

Henrichs v. Sundmaker, 405 Ill. 62, 89 N.E. 2d 732 (1950).

2. Where a partnership is charged with a breach of trust of a partner, the plaintiff must prove that the partners had knowledge of the breach of trust or that they participated in the breach of trust. Penn v. Fogler, 182 Ill. 76 (1899).

3. The plaintiff must also prove, in an action against a partnership arising out of a partner's breach of trust, that the defendants possessed knowledge of facts that would lead a reasonably intelligent and diligent person to make inquiry as to whether the trustees were committing a breach of trust. Kurowski v. Burch, 8 Ill. App. 3d 716, 720 (1972).

4. In the present case, the plaintiff has failed to prove by clear convincing and unequivocal evidence that the defendants had actual knowledge of Paul's breach of trust nor did the plaintiff prove that the defendants participated in this breach or that they were in possession of facts which would lead them to inquire whether Paul had in fact breached his duties as a fiduciary.

Count II, Plaintiff's Conspiracy Claim

5. In a claim alleging a civil conspiracy, the plaintiff must prove his case by clear convincing evidence. ABC Trans. Nat. Etc. v. Aeronautics Forwarders, 90 Ill. App. 3d 817, 413 N.E. 2d 1299 (1980):

6. Where the evidence presented leads to inferences which are equally consistent with innocent conduct as with guilt, it is the court's duty to find that the conspiracy has not been proven. ABC Trans. Nat. Etc. v. Aeronautics Forwarders, 90 Ill. App. 3d 816, 413 N.E. 2d 1299 (1980).

7. A civil conspiracy has been defined as a "combination of two or more persons acting in concert to commit an unlawful act, or to commit a lawful act by an unlawful means, the principal element of which is an agreement between the parties to inflict a wrong against or injury upon another and an overt act that results in damage." Hampton v. Hanrahan, 600 F.2d 600, 620 (7th Cir. 1979).

8. The plaintiff has failed to prove by clear and convincing evidence the existence of an agreement, either express or implied, with Paul to commit an unlawful act or to commit a lawful act by an unlawful means.

9. The plaintiff has failed to prove by clear and convincing evidence the existence of an agreement between defendants, Paul, and Ringbloom to obtain loans from the State Bank of Clearing for the benefit of Braemoor Associates without disclosing Paul's financial interest in Braemoor Associates.

Count III, Plaintiff's Claim for Unjust Enrichment

10. The court finds that the plaintiff has abandoned its claim for unjust enrichment.

11. If the plaintiff had presented this claim in its findings of fact and conclusions of law, the court would refuse to impose a constructive trust for the reasons set forth in the

court's conclusions of law related to Count I.

For the foregoing reasons, the defendants' motion for involuntary dismissal of the plaintiff's claims pursuant to Rule 41(b), Fed. R. Civ. P. is GRANTED. The plaintiff's claims are hereby dismissed with prejudice.

It is so ordered.



Nicholas J. Bua
Judge, United States District Court

DATED: November 16, 1981

In the
United States Court of Appeals
For the Seventh Circuit

No. 81-3040

FEDERAL DEPOSIT INSURANCE CORPORATION,

Plaintiff-Appellant,

v.

BRAEMOOR ASSOCIATES, et al.,

Defendants-Appellees.

Appeal from the United States District Court for the
Northern District of Illinois, Eastern Division.
No. 76 C 3295—Nicholas J. Bua, Judge.

ARGUED JUNE 11, 1982—DECIDED AUGUST 13, 1982

Before WOOD and POSNER, *Circuit Judges*, and CAMP-
BEIL, *Senior District Judge*.*

POSNER, *Circuit Judge*. The Federal Deposit Insurance Corporation, as successor in interest to a defunct Illinois state bank, the State Bank of Clearing, brought this suit against Braemoor Associates, a joint venture, and against five individuals who are the surviving joint venturers in Braemoor, seeking to recover bank monies that the bank's president, Paul Bere, had funneled to Braemoor in breach of his fiduciary obligations to the bank. The asserted basis of federal jurisdiction over the suit is 12 U.S.C. § 1819 Fourth, which provides that "all

* Of the Northern District of Illinois.

suits of a civil nature at common law or in equity to which the [Federal Deposit Insurance] Corporation shall be a party shall be deemed to arise under the laws of the United States, and the United States district courts shall have original jurisdiction thereof, without regard to the amount in controversy" There was a bench trial, but at the close of the FDIC's case the defendants moved for dismissal of the complaint under Rule 41(b) of the Federal Rules of Civil Procedure, and the motion was granted.

We consider first, as we must though no party to this litigation has raised the question, whether the federal courts have jurisdiction over the subject matter of the litigation. Section 1819 Fourth excepts from its grant of jurisdiction to those courts any suit to which the FDIC "is a party in its capacity as receiver of a State bank and which involves only the rights or obligations of depositors, creditors, stockholders, and such State bank under State law" When the State Bank of Clearing was closed down, the Illinois banking commissioner appointed the FDIC as receiver, see Ill. Rev. Stat. 1981, ch. 17, § 370, and the FDIC accepted appointment pursuant to 12 U.S.C. § 1821(e). Had the FDIC brought this suit—a suit to impose a constructive trust by reason of Paul Bere's violation of his fiduciary obligations under state law—in its capacity as receiver, the proviso, quoted above, to the grant of federal jurisdiction in section 1819 Fourth would have prevented the FDIC from maintaining the suit in federal court, at least under that section, which is the only basis of federal jurisdiction alleged. *FDIC v. Sumner Financial Corp.*, 602 F.2d 670, 679-80 (5th Cir. 1979). The complaint goes on to allege, however, that the FDIC, in conformity with Illinois law, used its position as receiver to transfer to itself certain bank assets, including the bank's cause of action against the defendants, and that it is suing in its capacity as owner of those assets rather than in its capacity as receiver. These allegations have not been denied; nor is there any doubt that the FDIC has authority under federal law to obtain bank assets in this fashion. See 12 U.S.C. §§ 1821(e), 1823(e). And when the FDIC is suing

to realize on such assets there is federal jurisdiction under section 1819 Fourth. *FDIC v. Ashley*, 585 F.2d 157, 161-62 (6th Cir. 1978).

The only novelty is that the asset that the FDIC is suing to realize on in this case is a cause of action, rather than as in the usual case a note or other financial instrument. *Ashley* is some authority for the proposition that this makes no difference, because the court in *Ashley* mentioned that the assets that had been transferred to the FDIC included causes of action against the bank's directors, 555 F.2d at 160; but since the opinion contains no separate discussion of these assets, we cannot be certain that the court would have thought them enough to support federal jurisdiction over the suit. The difficulty with basing jurisdiction solely on such an asset is that the enforcement of a bank's cause of action is precisely the sort of thing that a receiver would do, and the receiver's action in transferring the cause of action to itself therefore seems like an effort—a rather transparent one at that—to get around the jurisdictional limitations in section 1819 Fourth.

But we think it is necessary to distinguish between a transfer for value and one not for value. If the FDIC purchased the claims of the State Bank of Clearing against these defendants that would be the bona fide acquisition of a genuine asset, and a suit to realize on that asset would not be a suit in the FDIC's capacity as a receiver. Cf. *Ashley*, *supra*, 585 F.2d at 162; *FDIC v. Godshall*, 558 F.2d 220, 223 (4th Cir. 1977). The complaint alleges, without contradiction, that the transfer of assets to the FDIC was in accordance with Illinois law and was consented to by the circuit court of Cook County; and we think it unlikely, to say the least, that the circuit court would have allowed the FDIC to pocket assets of the State Bank of Clearing without giving anything in return. We find nothing in the Illinois Banking Act that would authorize such conduct. See Ill. Rev. Stat. 1981, ch. 17, §§ 372-73. We also think there is no question of the assignability of the bank's claim to the FDIC. See *Pattiz v. Semple*, 12 F.2d 276 (E.D. Ill. 1926), *aff'd*, 18 F.2d 955 (7th Cir. 1927). Of course it is possible that the

jurisdictional allegations are a lie—that the FDIC and the defendants are colluding to confer jurisdiction on the federal courts in contravention of the limitations in section 1819 Fourth—but we do not think that our obligation to police the limitations on our jurisdiction requires us to investigate such a hypothesis. We conclude that we have jurisdiction, though we deprecate the FDIC's failure to allege more fully the facts establishing federal jurisdiction.

There is another threshold issue not raised by the parties, and though it does not go to subject-matter jurisdiction we shall consider it on our own initiative. It is whether the substantive law to be applied in this case is federal common law or state law (if the latter, the state whose law applies is clearly Illinois). From the predominance of Illinois citations in the briefs and in the district court's conclusions of law we infer that the parties and the district court assumed that Illinois law supplied the rule of decision; but they did not say so, and it is at least possible, in light of the language of 12 U.S.C. § 1819 Fourth and certain judicial decisions, that they thought federal common law applied but was identical to Illinois law.

We expressed recently and remark once again our queasiness at being asked to decide an appeal without being told by the district court what substantive law to apply—state or federal, and if the former which state's law it is. *Central Soya Co. v. Epstein Fisheries, Inc.*, 676 F.2d 939, 941 (7th Cir. 1982). In some cases insistence on an explicit statement of the source of law would be pedantic, but not here. Maybe the "arising under" language of section 1819 Fourth is just a redundant way of conferring jurisdiction on the federal courts rather than a direction to those courts to create a common law of rights and obligations of the FDIC; but an unbroken line of decisions beginning with *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942), holds that the substantive law to be applied in suits to which the FDIC is a party is indeed federal common law, not state law. See *FDIC v. Timbalier Towing Co.*, 497 F. Supp. 912, 918 (N.D. Ohio 1980), and cases cited there. When the FDIC is

suing as a receiver appointed under state law the applicable substantive law is state rather than federal. *FDIC v. Leach*, 525 F. Supp. 1379, 1384 (E.D. Mich. 1981), but as we have pointed out this is not such a suit and could not be brought in federal court if it were.

However, the *D'Oench* line of cases is not so devastating to the approach taken below as might appear. As we noted recently in considering a related question—whether state or federal common law should supply the rule of decision for cases involving the construction of U.S. Postal Service leases—one choice for the federal common law judge is to adopt local law as the rule of decision. *Powers v. United States Postal Serv.*, 671 F.2d 1041, 1043 (7th Cir. 1982). That choice is attractive in the present case given the nature of the FDIC's claim.

The FDIC is suing as the assignee of the State Bank of Clearing's cause of action under state law against the defendants, and it is difficult to see why assignment to the FDIC should alter or enlarge that cause of action. *D'Oench*, though the Supreme Court refused in that case to follow state law, does not support such a metamorphosis. In *D'Oench* the FDIC had lent money to a bank that it had insured, and had received a note as collateral; and the question on which the Court refused to follow state law was whether the FDIC was a holder in due course, so that it could collect on the note free of the defenses that the payor might have had against the original payee. *D'Oench* was thus a case involving the rights of the United States in contracts to which it is a party, and is one of several cases all decided at about the same time that suggest that the rule of decision in such cases should be federal rather than state. See *Clearfield Trust Co. v. United States*, 318 U.S. 363, 367 (1943); *United States v. County of Allegheny*, 322 U.S. 174, 183 (1944); *Priebe & Sons, Inc. v. United States*, 332 U.S. 407, 411 (1947). Whatever the contemporary vitality of these cases—on which see *In re Murdock Machine & Engineering Co. of Utah*, 620 F.2d 767, 772 (10th Cir. 1980), and *Powers v. United States Postal Serv.*, *supra*, 671 F.2d at 1045—they do not control the present case: it does not involve a contract to which the FDIC is a party.

True, the FDIC has a vital stake in any asset of a defunct bank that it has insured; the statute under which it operates contemplates the transfer of assets, presumably including causes of action, from such a bank to the FDIC, see 12 U.S.C. §§ 1823(d), (e); and *D'Oench* teaches that an asset can confer on its holder greater rights when it comes into the hands of the FDIC. These considerations, coupled with the language of section 1819 Fourth, suggest that in an appropriate case a federal court could reject state substantive law if that was necessary to protect the FDIC's interest in minimizing depositor losses which it must make good. But the absence of any ready-made federal common law in most of the areas of law in which it might be applied, and a general reluctance to displace state law without explicit statutory or constitutional direction to do so, support a presumption that state law is adequate and should be adopted by the federal court as the rule of decision. See *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 740 (1979); *Powers v. United States Postal Serv.*, *supra*, 671 F.2d at 1045. The presumption is un rebutted here, so we can turn at last to the merits.

Braemoor Associates was formed in 1970 by several individuals, including Paul Bere, the president and board chairman of the State Bank of Clearing, to develop real estate. (Bere died before this suit was brought, and neither he nor his estate is a defendant.) Between 1970 and 1972 Bere caused the bank to make nine loans, totaling more than \$500,000, to various of the joint venturers for use by Braemoor. These loans violated state law. Although it is not unlawful per se for an Illinois bank to make a loan to its officers, or to enterprises which the officers control or actively manage, such loans—if they exceed \$10,000, as each of the nine loans did—require the approval of the bank's board of directors, see Illinois Banking Act, § 37(1), Ill. Rev. Stat. 1981, ch. 17, § 347(1), and that approval was not sought or given for any of the loans. However, all these loans were eventually repaid to the bank and are not in issue here.

Ringbloom, a real estate entrepreneur with whom Paul Bere had extensive business dealings, owned a company called Western. Bere and Ringbloom agreed that Western would purchase some land owned by Braemoor but the terms of payment were left somewhat indefinite. Late in 1971 Braemoor found itself owing a \$60,000 installment payment to Seneca, a company whose president, Hulse, was one of the joint venturers in Braemoor, on a contract to build streets and sewers for Braemoor. Braemoor had less than \$2000 in its bank account. Bere asked Ringbloom to pay Braemoor \$60,000 on account of Western's land purchase so that Braemoor could pay Seneca, but Ringbloom said that Western did not have the money. Bere thereupon had the State Bank of Clearing lend Ringbloom \$60,000 and Ringbloom immediately made out a check drawn on Western's bank account in the State Bank of Clearing for the same amount, payable to Braemoor. Ringbloom handed the check to Bere, who gave it to Hulse, who deposited it in Braemoor's bank account. Braemoor then paid Seneca \$60,000. The \$60,000 loan from the State Bank of Clearing to Ringbloom was not submitted to or approved by the bank's board of directors. It is the first of the two loan transactions at issue in this case.

Several months later Braemoor needed to pay Seneca another installment on the street and sewer contract, this one for \$240,000, in order to get Seneca to release some lots that Braemoor wanted to sell. Braemoor had only \$16,000 in its bank account. Again Bere turned to Ringbloom, though Western was not due to make a payment to Braemoor on its land purchase agreement at that time. Again Western did not have the money, and again Bere stepped into the breach with a loan from his bank. This transaction was more intricate than the previous one. Bere had previously asked his brother, Lambert Bere, another of the joint venturers in Braemoor, to sign a note in blank payable to the State Bank of Clearing and to leave the note with him, Paul; and Lambert had done so. Paul now completed the note by making it out for \$417,000, and directed the bank to lend this amount to Lambert. The money was deposited in a joint

account maintained by Lambert and his wife at the State Bank of Clearing. A few days later Paul caused the entire amount to be transferred out of the account. At his direction, \$167,000 was used to pay off loans that one of Ringbloom's companies had gotten from the bank, and the other \$250,000 was deposited in Western's checking account at the bank. Western made out a check for \$240,000 to Braemoor on the same day. From that point on the transaction was handled identically to the \$60,000 loan.

The \$240,000 payment to Braemoor is the second transaction at issue in this case. Lambert testified that he was stunned to receive his July 1972 bank statement showing a credit and offsetting debits for \$417,000 and that he asked Paul about them but never received an explanation. The \$417,000 loan was not submitted to or approved by the bank's board of directors.

The \$60,000 loan to Western that found its way into Braemoor's pockets and the \$240,000 portion of the second loan that also found its way into Braemoor's pockets were made in violation of Paul Bere's fiduciary obligations to his bank under section 37(1) of the Illinois Banking Act; and the question is whether this breach of trust may be imputed to Braemoor. If so, it is not disputed that the FDIC may recover the proceeds of the breach in the hands of Braemoor; and since the principles of partnership law apply to joint ventures of individuals, *Smith v. Metropolitan Sanitary District of Greater Chicago*, 77 Ill. 2d 313, 318, 396 N.E.2d 524, 527 (1979), there is also no question that if Braemoor is liable so are the individual defendants.

The district court found that the FDIC had failed to prove that the defendants had either (1) actual knowledge of Paul Bere's breach of trust or (2) knowledge of such facts as would lead a reasonable man to inquire whether Bere was committing a breach of trust; and the court concluded that without such proof the FDIC could not prevail. The FDIC does not challenge the finding that the defendants had no actual knowledge of the breach of trust, but it argues that the finding that they had no constructive notice is clearly erroneous and that

in any event there are alternative grounds for recovering the monies sued for that have nothing to do with what the joint venturers, other than Paul Bere himself, may have known, so that the district court's legal conclusion is incorrect even if none of its factfindings is.

We need not decide whether either factfinding is clearly erroneous. The FDIC's right to recover the proceeds of the two payments to Braemoor under the provisions of the Uniform Partnership Act (adopted in Illinois) is independent of what the other joint venturers knew, or as reasonable men should have known, about Paul Bere's breach of trust. Although the district court did not discuss the defendants' liability under the Uniform Partnership Act, the defendants do not contend that this theory of liability was not before the district court and should not be considered by us.

A joint venture of individuals is subject to the Uniform Partnership Act, *Mobil Oil Corp. v. Hurwitz*, 63 Ill. App. 3d 430, 380 N.E.2d 49 (1978), as indeed the Braemoor joint venture agreement expressly recites. Section 12 of the Act, Ill. Rev. Stat. 1981, ch. 106½, § 12, provides that "the knowledge of the partner acting in the particular matter, acquired while a partner or then present to his mind, . . . operate[s] as . . . knowledge of the partnership, except in the case of a fraud on the partnership committed by or with the consent of that partner." Paul Bere, a partner in Braemoor, knew that in funneling \$300,000 of his bank's money to Braemoor through Ringbloom, Western, and Lambert Bere he was violating his fiduciary duty to the bank under section 37(1) of the Illinois Banking Act. Section 12 of the Uniform Partnership Act "imputed" that knowledge to the other joint venturers, which is to say made them and Braemoor, despite their lack of knowledge, fully liable for the breach of trust and hence constructive trustees of the proceeds of that breach for the benefit of the bank and its successor in interest, the FDIC, just as Paul Bere would have been if the FDIC had sued him. See *Howard v. Hamilton*, 28 N.C. App. 670, 675, 222 S.E.2d 913, 917 (1976). The exception in section 12 of the Uniform Partnership Act for frauds on the partner-

ship is not applicable to this case, because Paul Bere was committing fraud on behalf of rather than against the partnership. Cf. *Maclay v. Kelsey-Seybold Clinic*, 456 S.W.2d 229, 234 (Tex. Civ. App. 1970), *aff'd*, 466 S.W.2d 716, 719 (Tex. 1971); *Cenco Inc. v. Seidman & Seidman*, Nos. 81-2116, 81-2264, slip op. at 11-12 (7th Cir. March 26, 1982). We neither see, nor desire to concoct, any escape from the language of section 12. "The rule which imposes civil liability upon an 'innocent' partner for bad faith dealing of a co-partner is most pointedly applicable where the co-partner participates in the benefits derived from the dealing in bad faith." *Higgins v. Shenango Pottery Co.*, 256 F.2d 504, 509 (3d Cir. 1958), construing an identically worded predecessor provision to section 12.

We reach the same conclusion by an alternative route. Section 13 of the Uniform Partnership Act, Ill. Rev. Stat. 1981, ch. 106½, § 13, provides that "where, by any wrongful act or omission of any partner acting in the ordinary course of the business of the partnership, or with the authority of his co-partners, loss or injury is caused to any person, not being a partner in the partnership, . . . the partnership is liable therefor to the same extent as the partner so acting or omitting to act." There is no doubt that Paul Bere's violation of section 37(1) of the Illinois Banking Act caused an injury to the bank (and hence to its successor in interest, the FDIC), so that Braemoor is liable if Bere was acting either "in the ordinary course of [Braemoor's] business" or "with the authority of" the other joint venturers; and we think he was doing both. The nine loans made at Paul Bere's direction by the State Bank of Clearing to the individual joint venturers for the benefit of Braemoor show that Bere was acting in the ordinary course of Braemoor's business when he channeled bank money to Braemoor in violation of the Illinois Banking Act. This is perfectly clear with respect to the nine loans themselves and scarcely less so with respect to the two loans in issue here. The fact that the money went from the bank to Braemoor through Ringbloom and Western, or as in the second transaction through Ringbloom, Western, and Lambert Bere, rather than directly, is a detail.

They were transactions, "laundered" transactions to be sure, by which Paul channeled the bank's money to Braemoor; and the financing of Braemoor by the bank had become the ordinary course of business for Braemoor. Cf. *Zelman v. Boston Ins. Co.*, 4 Cal. App. 3d 15, 84 Cal. Rptr. 206 (1970).

We also think his partners authorized Paul Bere to channel bank money to Braemoor. They knew, from the eight of the nine loans that predated the two loans in issue, that Bere was channeling money from his bank to Braemoor, and they obviously approved, and thereby authorized, his doing so. We can imagine no theory under which Paul Bere was authorized to borrow upwards of \$500,000 from the bank directly for Braemoor but not to borrow additional sums indirectly, through Ringbloom and Western. Why should his co-venturers have cared what route the money followed from its source? This is not to say that the actual violation of the Illinois Banking Act was authorized; we accept the district court's finding that the other venturers did not know of any such violation. But section 13 of the Uniform Partnership Act requires only that the partner who commits the wrong be acting with the authorization of his partners when he does so—not that the violation itself be authorized, see *Elle v. Babbitt*, 488 P.2d 440, 446-47 (Ore. 1971)—and Paul Bere was acting with that authorization when he committed the violation; he was not off on some frolic of his own. As for the district court's finding that "the defendants did not impliedly delegate to Paul the authority to arrange financing for the purchase of the Braemoor properties," we do not understand its relevance. The loans in issue were not for the purchase of any properties; they were for a street and sewer system on property already owned by Braemoor.

There is nothing novel or exotic about the principles embodied in sections 12 and 13 of the Uniform Partnership Act or their application to the facts of this case. The two sections, section 13 especially, merely extend to partnerships familiar principles of agency law, among them the principle of *respondeat superior*, whereby an

employer is liable for the torts of his employees committed in the course of their employment. The extension of this principle to partnerships antedates the Uniform Partnership Act. See *Hamlyn v. John Houston & Co.*, 1903 L.R. 1 K.B. 81 (C.A. 1902). The district court erred by limiting its analysis to the distinct principles that govern cases where property that has been obtained in breach of trust comes into the hands of a third party who is not the principal or agent or partner of the person who committed the breach or is otherwise linked to him by a preexisting relationship, but is a stranger, and the question is whether the stranger has sufficient notice of the breach of trust to be forced to disgorge the property. See *Kurowski v. Burch*, 8 Ill. App. 3d 716, 720, 290 N.E.2d 401, 405 (1972), *aff'd*, 57 Ill. 2d 292, 312 N.E.2d 284 (1974); Restatement of Restitution § 168(2) (1937); 4 Scott, *The Law of Trusts* §§ 296-97 (3d ed. 1967). The law imposes greater duties on people with regard to the acts of their agents and partners than with regard to the acts of strangers, presumably to give people an incentive to choose carefully with whom to enter into ventures that may injure innocent third parties.

So we need not consider whether the district court, treating this as if it were a case where the breaching trustee and the constructive trustee were strangers rather than partners, was correct in concluding as a matter of fact that the joint venturers lacked knowledge of such facts as would have led reasonable men to inquire further into whether Paul Bere was committing a breach of trust—though we shall not conceal our skepticism that Lambert Bere did all that a reasonable man should have done to inquire into the circumstances whereby \$417,000 passed mysteriously in and out of his bank account in a space of days. The liability of the joint venturers under the Uniform Partnership Act is independent of their knowledge—whether actual or, under general principles of restitution, constructive—of Paul Bere's breach of trust.

The FDIC has still another theory of liability—that the defendants conspired with Paul Bere to commit a

breach of trust against the bank. The district court rejected this theory on the facts, finding that the FDIC had failed to prove that the defendants actually knew of Bere's breach of trust. This finding is at least plausible; although they knew he was borrowing money from the bank for his joint venture his borrowing would not have been a breach of trust had Bere gotten the permission of his board of directors, a matter on which the defendants could not be presumed to be informed. At any rate we cannot say that the district court's finding was clearly erroneous, so we affirm this part of its judgment. However, the rejection of the FDIC's theory of liability under the Uniform Partnership Act was erroneous, and the judgment dismissing the complaint must therefore be reversed and the case remanded for further proceedings consistent with this opinion.

SO ORDERED.

A true Copy:

Teste:

*Clerk of the United States Court of
Appeals for the Seventh Circuit*

AMENDED
In the
United States Court of Appeals
For the Seventh Circuit

No. 81-3040

FEDERAL DEPOSIT INSURANCE CORPORATION,

Plaintiff-Appellant,

v.

BRAEMOOR ASSOCIATES, et al.,

Defendants-Appellees.

Appeal from the United States District Court for the
Northern District of Illinois, Eastern Division.
No. 76 C 3295—Nicholas J. Bua, Judge.

ARGUED JUNE 11, 1982—DECIDED AUGUST 13, 1982
AMENDED OCTOBER 28, 1982*

Before WOOD and POSNER, *Circuit Judges*, and CAMP-
BELL, *Senior District Judge*.**

POSNER, *Circuit Judge*. The Federal Deposit Insurance Corporation, as successor in interest to a defunct Illinois state bank, the State Bank of Clearing, brought this suit against Braemoor Associates, a joint venture, and against five individuals who are the surviving joint venturers in Braemoor, seeking to recover bank monies

* This amended opinion is issued in response to the petition for rehearing. In light of the amended opinion, the petition for rehearing is denied.

** Of the Northern District of Illinois.

that the bank's president, Paul Bere, had funneled to Braemoor in breach of his fiduciary obligations to the bank. The asserted basis of federal jurisdiction over the suit is 12 U.S.C. § 1819 Fourth, which provides that "all suits of a civil nature at common law or in equity to which the [Federal Deposit Insurance] Corporation shall be a party shall be deemed to arise under the laws of the United States, and the United States district courts shall have original jurisdiction thereof, without regard to the amount in controversy" There was a bench trial, but at the close of the FDIC's case the defendants moved for dismissal of the complaint under Rule 41(b) of the Federal Rules of Civil Procedure, and the motion was granted.

We consider first, as we must though no party to this litigation has raised the question, whether the federal courts have jurisdiction over the subject matter of the litigation. Section 1819 Fourth excepts from its grant of jurisdiction to those courts any suit to which the FDIC "is a party in its capacity as receiver of a State bank and which involves only the rights or obligations of depositors, creditors, stockholders, and such State bank under State law" When the State Bank of Clearing was closed down, the Illinois banking commissioner appointed the FDIC as receiver, see Ill. Rev. Stat. 1981, ch. 17, § 370, and the FDIC accepted appointment pursuant to 12 U.S.C. § 1821(e). Had the FDIC brought this suit—a suit to impose a constructive trust by reason of Paul Bere's violation of his fiduciary obligations under state law—in its capacity as receiver, the proviso, quoted above, to the grant of federal jurisdiction in section 1819 Fourth would have prevented the FDIC from maintaining the suit in federal court, at least under that section, which is the only basis of federal jurisdiction alleged. *FDIC v. Sumner Financial Corp.*, 602 F.2d 670, 679-80 (5th Cir. 1979). The complaint goes on to allege, however, that the FDIC, in conformity with Illinois law, used its position as receiver to transfer to itself certain bank assets, including the bank's cause of action against the defendants, and that it is suing in its capacity as owner of those assets rather than in its capacity as receiver. These allegations have not been denied; nor is

there any doubt that the FDIC has authority under federal law to obtain bank assets in this fashion. See 12 U.S.C. §§ 1821(e), 1823(e). And when the FDIC is suing to realize on such assets there is federal jurisdiction under section 1819 Fourth. *FDIC v. Ashley*, 585 F.2d 157, 161-62 (6th Cir. 1978).

The only novelty is that the asset that the FDIC is suing to realize on in this case is a cause of action, rather than as in the usual case a note or other financial instrument. *Ashley* is some authority for the proposition that this makes no difference, because the court in *Ashley* mentioned that the assets that had been transferred to the FDIC included causes of action against the bank's directors, 555 F.2d at 160; but since the opinion contains no separate discussion of these assets, we cannot be certain that the court would have thought them enough to support federal jurisdiction over the suit. The difficulty with basing jurisdiction solely on such an asset is that the enforcement of a bank's cause of action is precisely the sort of thing that a receiver would do, and the receiver's action in transferring the cause of action to itself therefore seems like an effort—a rather transparent one at that—to get around the jurisdictional limitations in section 1819 Fourth.

But we think it is necessary to distinguish between a transfer for value and one not for value. If the FDIC purchased the claims of the State Bank of Clearing against these defendants that would be the bona fide acquisition of a genuine asset, and a suit to realize on that asset would not be a suit in the FDIC's capacity as a receiver. Cf. *Ashley*, *supra*, 585 F.2d at 162; *FDIC v. Godshall*, 558 F.2d 220, 223 (4th Cir. 1977). The complaint alleges, without contradiction, that the transfer of assets to the FDIC was in accordance with Illinois law and was consented to by the circuit court of Cook County; and we think it unlikely, to say the least, that the circuit court would have allowed the FDIC to pocket assets of the State Bank of Clearing without giving anything in return. We find nothing in the Illinois Banking Act that would authorize such conduct. See Ill. Rev. Stat. 1981, ch. 17, §§ 372-73. We also think there is no question of the assignability of the bank's claim to the FDIC. See

Pattiz v. Semple, 12 F.2d 276 (E.D. Ill. 1926), *aff'd*, 18 F.2d 955 (7th Cir. 1927). Of course it is possible that the jurisdictional allegations are a lie—that the FDIC and the defendants are colluding to confer jurisdiction on the federal courts in contravention of the limitations in section 1819 Fourth—but we do not think that our obligation to police the limitations on our jurisdiction requires us to investigate such a hypothesis. We conclude that we have jurisdiction, though we deprecate the FDIC's failure to allege more fully the facts establishing federal jurisdiction.

There is another threshold issue not raised by the parties, and though it does not go to subject-matter jurisdiction we shall consider it on our own initiative. It is whether the substantive law to be applied in this case is federal common law or state law (if the latter, the state whose law applies is clearly Illinois). From the predominance of Illinois citations in the briefs and in the district court's conclusions of law we infer that the parties and the district court assumed that Illinois law supplied the rule of decision; but they did not say so, and it is at least possible, in light of the language of 12 U.S.C. § 1819 Fourth and certain judicial decisions, that they thought federal common law applied but was identical to Illinois law.

We expressed recently and remark once again our queasiness at being asked to decide an appeal without being told by the district court what substantive law to apply—state or federal, and if the former which state's law it is. *Central Soya Co. v. Epstein Fisheries, Inc.*, 676 F.2d 939, 941 (7th Cir. 1982). In some cases insistence on an explicit statement of the source of law would be pedantic, but not here. Maybe the "arising under" language of section 1819 Fourth is just a redundant way of conferring jurisdiction on the federal courts rather than a direction to those courts to create a common law of rights and obligations of the FDIC; but an unbroken line of decisions beginning with *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942), holds that the substantive law to be applied in suits to which the FDIC is a party is indeed federal common law, not state law. See *FDIC v. Timbalier Towing Co.*, 497 F. Supp. 912, 918 (N.D. Ohio 1980), and cases cited there. When the FDIC is

suing as a receiver appointed under state law the applicable substantive law is state rather than federal, *FDIC v. Leach*, 525 F. Supp. 1379, 1384 (E.D. Mich. 1981), but as we have pointed out this is not such a suit and could not be brought in federal court if it were.

However, the *D'Oench* line of cases is not so devastating to the approach taken below as might appear. As we noted recently in considering a related question—whether state or federal common law should supply the rule of decision for cases involving the construction of U.S. Postal Service leases—one choice for the federal common law judge is to adopt local law as the rule of decision. *Powers v. United States Postal Serv.*, 671 F.2d 1041, 1043 (7th Cir. 1982). That choice is attractive in the present case given the nature of the FDIC's claim.

The FDIC is suing as the assignee of the State Bank of Clearing's cause of action under state law against the defendants, and it is difficult to see why assignment to the FDIC should alter or enlarge that cause of action. *D'Oench*, though the Supreme Court refused in that case to follow state law, does not support such a metamorphosis. In *D'Oench* the FDIC had lent money to a bank that it had insured, and had received a note as collateral; and the question on which the Court refused to follow state law was whether the FDIC was a holder in due course, so that it could collect on the note free of the defenses that the payor might have had against the original payee. *D'Oench* was thus a case involving the rights of the United States in contracts to which it is a party, and is one of several cases all decided at about the same time that suggest that the rule of decision in such cases should be federal rather than state. See *Clearfield Trust Co. v. United States*, 318 U.S. 363, 367 (1943); *United States v. County of Allegheny*, 322 U.S. 174, 183 (1944); *Priebe & Sons, Inc. v. United States*, 332 U.S. 407, 411 (1947). Whatever the contemporary vitality of these cases—on which see *In re Murdock Machine & Engineering Co. of Utah*, 620 F.2d 767, 772 (10th Cir. 1980), and *Powers v. United States Postal Serv.*, *supra*, 671 F.2d at 1045—they do not control the present case: it does not involve a contract to which the FDIC is a party.

True, the FDIC has a vital stake in any asset of a defunct bank that it has insured; the statute under which it operates contemplates the transfer of assets, presumably including causes of action, from such a bank to the FDIC, see 12 U.S.C. §§ 1823(d), (e); and *D'Oench* teaches that an asset can confer on its holder greater rights when it comes into the hands of the FDIC. These considerations, coupled with the language of section 1819 Fourth, suggest that in an appropriate case a federal court could reject state substantive law if that was necessary to protect the FDIC's interest in minimizing depositor losses which it must make good. But the absence of any ready-made federal common law in most of the areas of law in which it might be applied, and a general reluctance to displace state law without explicit statutory or constitutional direction to do so, support a presumption that state law is adequate and should be adopted by the federal court as the rule of decision. See *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 740 (1979); *Powers v. United States Postal Serv.*, *supra*, 671 F.2d at 1045. The presumption is un rebutted here, so we can turn at last to the merits.

Braemoor Associates was formed in 1970 by several individuals, including Paul Bere, the president and board chairman of the State Bank of Clearing, to develop real estate. (Bere died before this suit was brought, and neither he nor his estate is a defendant.) Between 1970 and 1972 Bere caused the bank to make nine loans, totaling more than \$500,000, to various of the joint venturers for use by Braemoor. These loans violated state law. Although it is not unlawful per se for an Illinois bank to make a loan to its officers, or to enterprises which the officers control or actively manage, such loans, if they exceed \$10,000, as each of the nine loans did, require the approval of the bank's board of directors, see Illinois Banking Act, § 37(1), Ill. Rev. Stat. 1981, ch. 17, § 347(1), and implicitly therefore disclosure of the conflict of interest to the board. Since that disclosure was not made, the board's approval of these loans, an approval procured by fraud, was ineffective. However, all these loans were eventually repaid to the bank and are not in issue here.

Ringbloom, a real estate entrepreneur with whom Paul Bere had extensive business dealings, owned a company called Western. Bere and Ringbloom agreed that Western would purchase some land owned by Braemoor but the terms of payment were left somewhat indefinite. Late in 1971 Braemoor found itself owing a \$60,000 installment payment to one of its contractors. Braemoor had less than \$2000 in its bank account. Bere asked Ringbloom to pay Braemoor \$60,000 on account of Western's land purchase so that Braemoor could pay the contractor, but Ringbloom said that Western did not have the money. Bere thereupon had the State Bank of Clearing lend Ringbloom \$60,000 and Ringbloom immediately made out a check drawn on Western's bank account in the State Bank of Clearing for the same amount, payable to Braemoor. Ringbloom handed the check to Bere, who had it deposited in Braemoor's bank account. Braemoor then paid the contractor \$60,000. The fact that the actual destination of the \$60,000 loan from the State Bank of Clearing to Ringbloom was an enterprise controlled by Bere was not disclosed to the bank's board of directors. It is the first of the two loan transactions at issue in this case.

Several months later Braemoor needed to pay another installment to one of its contractors, this one for \$240,000. Braemoor had only \$16,000 in its bank account. Again Bere turned to Ringbloom, though Western was not due to make a payment to Braemoor on its land purchase agreement at that time. Again Western did not have the money, and again Bere stepped into the breach with a loan from his bank. This transaction was more intricate than the previous one. Bere had previously asked his brother, Lambert Bere, another of the joint venturers in Braemoor, to sign a note in blank payable to the State Bank of Clearing and to leave the note with him, Paul; and Lambert had done so. Paul now completed the note by making it out for \$417,000, and directed the bank to lend this amount to Lambert. The money was deposited in a joint account maintained by Lambert and his wife at the State Bank of Clearing. A few days later Paul caused the entire amount to be transferred out of the account.

At his direction, \$167,000 was used to pay off loans that one of Ringbloom's companies had gotten from the bank, and the other \$250,000 was deposited in Western's checking account at the bank. Western made out a check for \$240,000 to Braemoor on the same day. From that point on the transaction was handled identically to the \$60,000 loan.

The \$240,000 payment to Braemoor is the second transaction at issue in this case. Lambert testified that he was stunned to receive his July 1972 bank statement showing a credit and offsetting debits for \$417,000 and that he asked Paul about them but never received an explanation. The actual destination of the \$417,000 loan was again not disclosed to the bank's board of directors.

The \$60,000 loan to Western that found its way into Braemoor's pockets and the \$240,000 portion of the second loan that also found its way into Braemoor's pockets were made in violation of Paul Bere's fiduciary obligations to his bank under section 37(1) of the Illinois Banking Act; and the question is whether this breach of trust may be imputed to Braemoor. If so, it is not disputed that the FDIC may recover the proceeds of the breach in the hands of Braemoor; and since the principles of partnership law apply to joint ventures of individuals, *Smith v. Metropolitan Sanitary District of Greater Chicago*, 77 Ill. 2d 313, 318, 396 N.E.2d 524, 527 (1979), there is also no question that if Braemoor is liable so are the individual defendants.

The district court found that the FDIC had failed to prove that the defendants had either (1) actual knowledge of Paul Bere's breach of trust or (2) knowledge of such facts as would lead a reasonable man to inquire whether Bere was committing a breach of trust; and the court concluded that without such proof the FDIC could not prevail. The FDIC does not challenge the finding that the defendants had no actual knowledge of the breach of trust, but it argues that the finding that they had no constructive notice is clearly erroneous and that in any event there are alternative grounds for recovering the monies sued for that have nothing to do with what the joint venturers, other than Paul Bere himself,

may have known, so that the district court's legal conclusion is incorrect even if none of its factfindings is.

We need not decide whether either factfinding is clearly erroneous. The FDIC's right to recover the proceeds of the two payments to Braemoor under the provisions of the Uniform Partnership Act (adopted in Illinois) is independent of what the other joint venturers knew, or as reasonable men should have known, about Paul Bere's breach of trust. Although the district court did not discuss the defendants' liability under the Uniform Partnership Act, the defendants do not contend that this theory of liability was not before the district court and should not be considered by us.

A joint venture of individuals is subject to the Uniform Partnership Act, *Mobil Oil Corp. v. Hurwitz*, 63 Ill. App. 3d 430, 380 N.E.2d 49 (1978), as indeed the Braemoor joint venture agreement expressly recites. Section 12 of the Act, Ill. Rev. Stat. 1981, ch. 106½, § 12, provides that "the knowledge of the partner acting in the particular matter, acquired while a partner or then present to his mind, . . . operate[s] as . . . knowledge of the partnership, except in the case of a fraud on the partnership committed by or with the consent of that partner." Paul Bere, a partner in Braemoor, knew that in funneling \$300,000 of his bank's money to Braemoor through Ringbloom, Western, and Lambert Bere he was violating his fiduciary duty to the bank under section 37(1) of the Illinois Banking Act. Section 12 of the Uniform Partnership Act "imputed" that knowledge to the other joint venturers, which is to say made them and Braemoor, despite their lack of knowledge, fully liable for the breach of trust and hence constructive trustees of the proceeds of that breach for the benefit of the bank and its successor in interest, the FDIC, just as Paul Bere would have been if the FDIC had sued him. See *Howard v. Hamilton*, 28 N.C. App. 670, 675, 222 S.E.2d 913, 917 (1976). The exception in section 12 of the Uniform Partnership Act for frauds on the partnership is not applicable to this case, because Paul Bere was committing fraud on behalf of rather than against the partnership. Cf. *Maclay v. Kelsey-Seybold Clinic*,

456 S.W.2d 229, 234 (Tex. Civ. App. 1970), *aff'd*, 466 S.W.2d 716, 719 (Tex. 1971); *Cenco Inc. v. Seidman & Seidman*, 686 F.2d 449, 454-56 (7th Cir. 1982). We neither see, nor desire to concoct, any escape from the language of section 12. "The rule which imposes civil liability upon an 'innocent' partner for bad faith dealing of a co-partner is most pointedly applicable where the co-partner participates in the benefits derived from the dealing in bad faith." *Higgins v. Shenango Pottery Co.*, 256 F.2d 504, 509 (3d Cir. 1958), construing an identically worded predecessor provision to section 12.

We reach the same conclusion by an alternative route. Section 13 of the Uniform Partnership Act, Ill. Rev. Stat. 1981, ch. 106½, § 13, provides that "where, by any wrongful act or omission of any partner acting in the ordinary course of the business of the partnership, or with the authority of his co-partners, loss or injury is caused to any person, not being a partner in the partnership, . . . the partnership is liable therefor to the same extent as the partner so acting or omitting to act." There is no doubt that Paul Bere's violation of section 37(1) of the Illinois Banking Act caused an injury to the bank (and hence to its successor in interest, the FDIC), so that Braemoor is liable if Bere was acting either "in the ordinary course of [Braemoor's] business" or "with the authority of" the other joint venturers; and we think he was doing both. The nine loans made at Paul Bere's direction by the State Bank of Clearing to the individual joint venturers for the benefit of Braemoor show that Bere was acting in the ordinary course of Braemoor's business when he channeled bank money to Braemoor in violation of the Illinois Banking Act. This is perfectly clear with respect to the nine loans themselves and scarcely less so with respect to the two loans in issue here. The fact that the money went from the bank to Braemoor through Ringbloom and Western, or as in the second transaction through Ringbloom, Western, and Lambert Bere, rather than directly, is a detail. They were transactions, "laundered" transactions to be sure, by which Paul channeled the bank's money to Braemoor; and the financing of Braemoor by the bank had become the ordinary course of business for Brae-

moor. Cf. *Zemelman v. Boston Ins. Co.*, 4 Cal. App. 3d 15, 84 Cal. Rptr. 206 (1970).

We also think his partners authorized Paul Bere to channel bank money to Braemoor. They knew, from the eight of the nine loans that predated the two loans in issue, that Bere was channeling money from his bank to Braemoor, and they obviously approved, and thereby authorized, his doing so. We can imagine no theory under which Paul Bere was authorized to borrow upwards of \$500,000 from the bank directly for Braemoor but not to borrow additional sums indirectly, through Ringbloom and Western. Why should his co-venturers have cared what route the money followed from its source? This is not to say that the actual violation of the Illinois Banking Act was authorized; we accept the district court's finding that the other venturers did not know of any such violation. But section 13 of the Uniform Partnership Act requires only that the partner who commits the wrong be acting with the authorization of his partners when he does so—not that the violation itself be authorized, see *Elle v. Babbitt*, 488 P.2d 440, 446-47 (Ore. 1971)—and Paul Bere was acting with that authorization when he committed the violation; he was not off on some frolic of his own. As for the district court's finding that "the defendants did not impliedly delegate to Paul the authority to arrange financing for the purchase of the Braemoor properties," we do not understand its relevance. The loans in issue were not for the purchase of any properties; they were for a street and sewer system on property already owned by Braemoor.

There is nothing novel or exotic about the principles embodied in sections 12 and 13 of the Uniform Partnership Act or their application to the facts of this case. The two sections, section 13 especially, merely extend to partnerships familiar principles of agency law, among them the principle of *respondeat superior*, whereby an employer is liable for the torts of his employees committed in the course of their employment. The extension of this principle to partnerships antedates the Uniform Partnership Act. See *Hamlyn v. John Houston & Co.*, 1903

L.R. 1 K.B. 81 (C.A. 1902). The district court erred by limiting its analysis to the distinct principles that govern cases where property that has been obtained in breach of trust comes into the hands of a third party who is not the principal or agent or partner of the person who committed the breach or is otherwise linked to him by a preexisting relationship, but is a stranger, and the question is whether the stranger has sufficient notice of the breach of trust to be forced to disgorge the property. See *Kurowski v. Burch*, 8 Ill. App. 3d 716, 720, 290 N.E.2d 401, 405 (1972), *aff'd*, 57 Ill. 2d 292, 312 N.E.2d 284 (1974); Restatement of Restitution § 168(2) (1937); 4 Scott, *The Law of Trusts* §§ 296-97 (3d ed. 1967). The law imposes greater duties on people with regard to the acts of their agents and partners than with regard to the acts of strangers, presumably to give people an incentive to choose carefully with whom to enter into ventures that may injure innocent third parties.

So we need not consider whether the district court, treating this as if it were a case where the breaching trustee and the constructive trustee were strangers rather than partners, was correct in concluding as a matter of fact that the joint venturers lacked knowledge of such facts as would have led reasonable men to inquire further into whether Paul Bere was committing a breach of trust—though we shall not conceal our skepticism that Lambert Bere did all that a reasonable man should have done to inquire into the circumstances whereby \$417,000 passed mysteriously in and out of his bank account in a space of days. The liability of the joint venturers under the Uniform Partnership Act is independent of their knowledge—whether actual or, under general principles of restitution, constructive—of Paul Bere's breach of trust.

The FDIC has still another theory of liability—that the defendants conspired with Paul Bere to commit a breach of trust against the bank. The district court rejected this theory on the facts, finding that the FDIC had failed to prove that the defendants actually knew of Bere's breach of trust. This finding is at least plausible;

although they knew he was borrowing money from the bank for his joint venture his borrowing would not have been a breach of trust had Bere gotten the informed consent of his board of directors, a matter about which the defendants could not be presumed to know. At any rate we cannot say that the district court's finding was clearly erroneous, so we affirm this part of its judgment. However, the rejection of the FDIC's theory of liability under the Uniform Partnership Act was erroneous, and the judgment dismissing the complaint must therefore be reversed and the case remanded for further proceedings consistent with this opinion.

SO ORDERED.

A true Copy:

Teste:

*Clerk of the United States Court of
Appeals for the Seventh Circuit*